not be mandated. Rather additional points of interconnection should be negotiated on an individual case basis, where proper consideration can be given to the technical, engineering, administrative and operational requirements at the specific location where interconnection is being requested.

If further local loop unbundling were mandated on a national basis, it would have a major technical and operational impact in several areas, including the location of potential points of interconnection, (e.g., manholes, controlled environmental vaults (CEVs), splice cases, crossboxes, distribution terminals, or other wire connection points). In each of these locations, there may be limited, if any, space to accommodate additional cable facilities or interconnect devices. In some instances, any attempt to introduce additional cable sheaths would further reduce available space and seriously impair the LEC's ability to perform work. Trouble shooting will become more complex and costly. In most cases, testing and clearing problems will require a coordinated effort. All these factors will impact the quality of service provided to the consumer.

The ability to provide multiple access at intermediate points in the loop is also significantly affected by the design of the hardware used in these locations. As with the network as a whole, this equipment was not intended or designed to be accessed and used by multiple network providers. The ability to provide access and interconnection is further complicated by the mix of hardware and vintages of the equipment.

Mandated unbundling of sub-loop elements would also have a major impact on the operational support systems used in this area of the network. Massive changes would be required in order to manage and track which facilities are assigned and connected to the various network providers. This substantial effort would include changes required to inventory points of interconnection, the redesign of operation support systems, and the re-engineering of administrative, planning and provisioning processes. More importantly, mandating sub-loop unbundling has the potential to freeze technology. If the local loop is unbundled into multiple elements with multiple interconnection points, the incumbent LEC's flexibility to change out technology will be greatly hampered. In those cases where the incumbent LEC has legitimate reasons for changing out its technology, additional costs will be incurred by both the incumbent LEC and the interconnectors. In many instances, interconnectors will resist the change and seek to maintain the existing technology and arrangements. Others may position the change as an anti-competitive tactic intended to interfere with their operations. The Commission should therefore not mandate unbundling of sub-loop elements. Instead, the Commission should allow LECs to negotiate with requesting carriers the specific requirements and location(s) for intermediate points of loop interconnection.

D. <u>Switch Unbundling</u>

The Commission requests comment on proposals for unbundling switching. The primary function of a LEC switch is to connect lines in the most efficient and economical manner in order to establish the communications path desired by the subscriber. NYNEX currently offers CLECs an unbundled switch port which is the physical piece of equipment on the switch to which a customer's individual loop is connected.[134] The port provides, within specific operating parameters, access to basic switching features, such as dial tone, and to optional calling

[134] If a switch is connected to 10,000 lines, it has 10,000 line ports.

features and capabilities (e.g., call waiting). A port by itself, however, has no utility. It is, however, necessary for gaining access to the switch's various functions. Thus, the port and switch are, in reality, not severable.

In the NPRM, the Commission expresses concern about the manner in which NYNEX charged for the "switching" associated with its unbundled ports.[135] NYNEX believes that it is technically feasible to establish a port/switching element with a usage sensitive rate that would allow CLECs to offer the services they desire without paying for switching usage based on NYNEX retail service charges. This approach would not require the unnecessary and unuseful separation of ports from the switch.

NYNEX does not believe that the approach to unbundling switching discussed in paragraphs 100 and 102 of the NPRM is appropriate. Such an approach would create operational and service quality difficulties resulting from the unmanageable contention for the shared and limited resources of the switch. These common resources include switching paths, call processing and memory capacity, and logical assets such as routing tables. The unbundling approach discussed in paragraphs 100 and 102 of the NPRM provides no way to partition, allocate and administer these shared resources in a manner that meets the needs of the interconnector while ensuring service quality for all others that share those resources. On the other hand, the unbundled port/switching element does provide a means to negotiate the allocation of these resources effectively. While NYNEX believes that its approach to unbundling

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[135] Currently, NYNEX charges CLECs that utilize unbundled ports retail service charges for switching.

switching is more than adequate, other approaches to unbundling switching should be left to negotiations with requesting parties.

E. Databases and Signaling Systems

NYNEX currently provides unbundled access to its signaling systems and databases. Today, with its Signaling System 7 (SS7) network, NYNEX provides unbundled access to network signaling resources for call set up and for 800 and LIDB database queries through unbundled links and ports at its STPs. The STP provides a secure, manageable access to these physical resources and logical functions. As has been shown in the Intelligent Network proceeding, allowing third parties to access other elements of the SS7 network (such as the SCP databases) could have a significant impact on network reliability, CLEC and LEC service performance, and the security of interconnector and LEC network information.

The Commission should not adopt more detailed unbundling rules related to databases and Signaling Systems. Alternative suppliers of these functions exist today and as the market grows additional suppliers will enter.[136] The level of unbundling addressed above is all that is needed to further advance competition. Additional unbundling should be left to individual negotiations and the competitive marketplace. More detailed requirements may adversely impact the availability of these alternative providers by displacing competitive entry.

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[136] The Commission correctly notes (NPRM, ¶ 110) that there are alternative suppliers of call set up services other than the incumbent LECs.

IX. THE COMMISSION SHOULD ALLOW RESTRICTIONS ON RESALE

In this section, we address issues related to a LEC's duty to make certain services available for resale and to offer them to resellers at wholesale rates. The relevant sections of the Act are §§ 251(b)(1), 251(c)(4), and 252(d)(3).

Section 251(b)(1) of the Act provides:

> "Each local exchange carrier has the following duties: . . . The duty not to prohibit, and not to impose unreasonable or discriminatory conditions or limitations on, the resale of its telecommunications services."

Incumbent local exchange carriers have the following additional duties with respect to resale:

> "The duty — (A) to offer for resale at wholesale rates any telecommunications service that the carrier provides at retail to subscribers who are not telecommunications carriers; and (B) not to prohibit, and not to impose unreasonable or discriminatory conditions or limitations on, the resale of such telecommunications service, except that a State commission may, consistent with regulations prescribed by the Commission under this section, prohibit a reseller that obtains at wholesale rates a telecommunications service that is available at retail only to a category of subscribers form offering such service to a different category of subscribers."[137]

The pricing standard for services "offer[ed] for resale at wholesale rates" under § 251(c)(4) is set forth in § 252(d)(3):

> "For the purposes of section 251(c)(4), a State commission shall determine wholesale rates on the basis of retail rates charged to subscribers for the telecommunications service requested, excluding the portion thereof attributable to any marketing, billing, collection, and other costs that will be avoided by the local exchange carrier."

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[137] § 251(c)(4).

A. General Scope Of §§ 251(b)(1) And (c)(4)

The only requirement imposed by § 251(b)(1) is that a LEC may not impose unreasonable restrictions or limitations on the resale of "its telecommunications services" by entities that might purchase those services. Thus, that section does not require LECs to develop new services for the benefit of resellers, or to modify or unbundle its existing services. A LEC fully fulfills its obligations under § 251(b)(1) if it allows a reseller to purchase the LEC's existing telecommunications services at the existing terms, conditions and prices, and if it does not impose unreasonable restrictions on the resale of those services by the purchaser. Moreover, a LEC is free under § 251(b)(1) to withdraw or modify its retail offerings without any special restrictions or notice requirements (other than the generally applicable requirements imposed under State law). To do otherwise would unfairly lock incumbent LECs into unprofitable or otherwise non-market-oriented retail offerings, and would impose unfair competitive burdens on them. Nor would such a requirement be necessary to ensure fair competition between resellers and incumbents.

Although § 251(c)(4) does require incumbent LECs to offer services to resellers at "wholesale" rates, the only services to which that obligation applies are those that the incumbent "provides at retail" to non-carrier subscribers. Thus, like § 251(b)(1), § 251(c)(4) does not require LECs to custom-design special services for resellers, nor does it prohibit them from withdrawing or modifying services at will. Moreover, because § 251(c)(4) is limited to *retail* services, incumbent LECs are not required to offer for resale at wholesale rates: network elements, wholesale services, or services available only to carriers. On the other hand, nothing precludes competitors that obtain incumbent LEC resale services from using these services to offer custom-designed services and pricing packages to their customers.

B. The Meaning Of "Resale"

Sections 251(b)(1) and (c)(4) only apply to services that are offered for resale. Although the term "resale" is not defined in the statute, its plain meaning nevertheless limits in important ways the scope of the obligations imposed by those two sections.

"Resale" means the sale to another person of products and services purchased from a LEC. Thus, a purchaser is not entitled to pay wholesale rates under § 251(c)(4) if it is purchasing a service for its own use rather than for sale to another. Consider, for example, an interexchange carrier purchasing exchange access service from an incumbent LEC. Such a carrier is *using* that service in the provisioning of a separate and distinct service; namely, the IC's inter- or intraLATA toll service. Such an arrangement cannot be considered resale, and the ICs would not be entitled to wholesale rates. An IC cannot properly be described as an access reseller any more than a baker could be considered a reseller of flour and sugar.

C. The Obligation to Make Services Available for Resale at Wholesale Rates Only Applies To Telecommunications Service

The obligations imposed by §§ 251(b)(1) and 251(c)(4) only apply to "telecommunications services." A telecommunications service is "the offering of telecommunications for a fee directly to the public"[138] and "telecommunications" means "the transmission, between or among points specified by the user, of information of the user's

[138] Communications Act § 153(46).

choosing, without change in the form or content of the information as sent and received."[139] Although these definitions are broad, they do not include, for example, enhanced or information services.[140] Those services are therefore not subject to the Act's resale obligations.

D. Other Services Not Subject To §§ 251(b)(1) Or § 251(c)(4)

Certain other services should be declared by the Commission not to be subject to the obligations imposed by §§ 251(b)(1) and 251(c)(4).

1. Grandfathered Services

"Grandfathered" services are those that are offered on a retail basis only to existing end user customers (at their existing premises), and not to any new end user customers. (Grandfathering allows a LEC to discontinue or modify the offering of an unprofitable service while protecting the possible reliance interests of customers who already use the service.) Resellers should not be able to evade tariff restrictions on grandfathered services, and to defeat the very purpose of grandfathering, by purchasing such services to offer them to non-grandfathered customers. Moreover, because it is not offered to "the public" but only to a limited class of existing customers, a grandfathered service cannot be regarded as a telecommunications service within the meaning of §§ 251(b)(1) or (c)(4).

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[139] See Sections 3(43) and (46).

[140] The legislative history of the definitions of telecommunications service make it clear that information services were not intended to be included in that definition. The House bill explicitly stated that the term "does not include an information service." See H.R. 1555, Section 501(a), proposed Section 153(50) of Communications Act. Although the Senate bill did not include such an express exclusion, the Senate report noted that "[t]elecommunications service" does not include information services, cable services, or 'wireless' cable services, but does include the transmission, without change in the form or content, of such services" (Senate Report at 18).

2. **Promotional Offerings**

New services are frequently introduced (and existing services are frequently marketed to new customers) through short-term waivers of recurring or non-recurring charges to new customers. Such waivers should be regarded as being in the nature of marketing programs for retail service offerings rather than retail service offerings in themselves, and we believe that each competitor should finance its own such programs. A contrary rule — one that would require the incumbent LEC to use the "promotional" price as a base price for wholesale pricing purposes — would in effect require a LEC to fund not only its own promotions but those of its competitors. This would deprive a LEC of much of its incentive to engage in promotions, and thus vitiate an important and pro-competitive marketing tool.

Moreover, the inherently short-term nature of such promotions would make it difficult to provide appropriate operational support for resale without impairing a LEC's ability to offer the promotions at retail on a timely basis. Again, the effect would be to deter the use of promotions. In short, imposing resale requirements on promotional offerings would suppress competition rather than enhance it.

In excluding promotional offerings from a LEC's resale obligation, we do not mean to suggest that services that are discounted on a more-or-less permanent basis, such as optional calling plans, should also be excluded. We believe that optional calling plans are actual retail services, and should be treated the same as any other services for resale purposes.[141] We also agree that special offerings priced on an individual case or customer-specific basis ("ICB" or "CSP" arrangements) should be subject to resale.[142]

However, like other retail services offered for resale, optional calling plans and ICB/CSP pricing arrangements must be accepted by resellers subject to the same terms and conditions as govern their offering to end user customers. For optional calling plans, these may include conditions related to the customer's current and prior levels of usage. Moreover, since an ICB/CSP price is offered only to a single customer, a reseller may only purchase an ICB/CSP offering for resale to the customer in question, or to another, similarly situated customer.

The NPRM asks how restrictions on the resale of optional calling plans "[would] be enforced without impeding competition (e.g., through disclosure of competitively sensitive information)" We do not believe that this presents any insuperable difficulties. Information provided by resellers to incumbent LECs for the purpose of qualifying their customers for certain pricing plans can be treated as confidential information which LEC reseller-service personnel would be restricted (with appropriate conditions and exceptions) from disclosing to the LEC's retail marketing personnel.

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141 The distinction between promotional offerings and discounted calling plans could most readily be drawn on the basis of the duration of the discount. We suggest a criterion of 90 days or less for promotional offerings.

142 Because of the somewhat customized manner in which they are developed and provided, there may be no avoided costs associated with the offering of ICB/CSP arrangements to resellers.

3. **Coin Phone Service**

By "coin phone service," we refer to retail public telephone service: that is, the service that is offered to the "man (or woman) on the street," and that gives that person the capability of making a call from a Company-owned public telephone. Thus, it is important to note that in excluding public coin telephone service from resale, we are not seeking to limit or in any way affect LEC obligations with respect to the provision of Public Access Lines or other products used by competitive payphone providers.

The offering of PAL lines and similar products from NYNEX has nurtured a highly successful competitive payphone industry. Indeed, in parts of New York City, competitive payphone penetration rates approach and even exceed fifty percent. The growth of that industry will undoubtedly be accelerated, and competitive payphone providers will be afforded additional safeguards, by the payphone provisions of the Act (Section 276). No one has suggested that the offering retail coin service itself for resale is necessary to the development of competition in this area.

Retail coin service differs in significant respects from other services that might be offered for resale at wholesale rates. When a LEC offers local exchange service to a reseller in bulk, instead of directly to end users, it may be able to able to avoid many of the costs associated with direct, person-to-person dealings between the LEC and its end user customers. Coin service, on the other hand, is not "ordered" by specific individuals through calls to LEC service representatives. Thus, offering retail coin service for resale would not enable the LEC to avoid any of the costs it incurs in dealing with its customers. Instead, it would merely add to its normal retail cost structure, the additional costs necessary to interface with resellers.

E. Other Reasonable Restrictions On Resale

Sections 251(b)(1) and (c)(4) only prohibit conditions or limitations on resale to the extent that they are "unreasonable" or "discriminatory." There is thus no statutory basis for the position that "there should be no prohibitions or restrictions on the resale of the services of dominant carriers."[143] Nor is there any warrant in the statute for narrowing the range of permissible restrictions beyond the explicit requirements of reasonableness and nondiscrimination.[144] The burden of demonstrating that a particular State-imposed restriction is unreasonable or discriminatory should be on the party making that claim.

In general, we believe that the Commission should defer to State determinations as to what types of restrictions are reasonable. This is necessary in view of the fact that resale restrictions are frequently imposed in order to protect State-mandated retail pricing policies. Since those policies are imposed by State commissions, those commissions should play the predominant role in ensuring that they are not undermined by resale.

One class of conditions that are manifestly reasonable and nondiscriminatory are "class of customer" restrictions, i.e., prohibitions on the resale of services to retail customers who

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[143] NPRM, ¶ 175n. 233 (referring to the views of ALTS, the Association for Local Telecommunications Services).

[144] See NPRM ¶ 175 (concluding that "the range of permissible restrictions should be quite narrow"). See also NPRM ¶ 197 ("few, if any conditions or limitations [upon resale] should be permitted because such restrictions generally are inconsistent with the pro-competitive thrust of the Act and would likely be evidence of the exercise of market power").

would not be permitted to purchase those service directly from the LEC. (An example would be a requirement that prohibited the sale of residence services to business customers.)[145] Indeed, State commissions are expressly permitted to authorize such restrictions by § 251(c)(4)(B).[146]

Such restrictions are particularly important in view of the fact that such limitations in retail tariffs frequently reflect mandated, below-market prices that are intended to protect (and thus are only offered to) particular classes of customers. Allowing resellers to ignore such restrictions would unfairly extend a LEC's regulatory obligations to offer "social policy based" prices to situations where the underlying social policy is inapplicable. Thus, to give an obvious example, resellers should not be permitted to resell LifeLine service to business customers.[147]

Another restriction that should be regarded as reasonable is a prohibition on the resale to multiple customers of a single flat-rated exchange service line purchased from a LEC. Such lines are priced based on estimated levels of usage or residually based on the number of flat-rate customers; prices set in this manner would become worthless if resellers were allowed to combine the usage of multiple customers on a single line.

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[145] Of course it is the reseller's end user customer, and not the reseller itself, that would be required to be within the class of allowed purchasers. Thus, a reseller, although a business customer, would be permitted to purchase a residence-only service; however, it would only be allowed to resell the service to residence customers.

[146] "[A] State commission may, consistent with regulations prescribed by the Commission under this section, prohibit a reseller that obtains at wholesale rates a telecommunications service that is available at retail only to a category of subscribers from offering such service to a different category of subscribers."

[147] Note that class of customer restrictions do not preclude purchase by resellers of high volume services and their resale to low volume customers within defined retail class.

X. ONLY NET AVOIDED COSTS SHOULD BE EXCLUDED FROM THE PRICING OF SERVICES OFFERED FOR RESALE UNDER SECTIONS 251(c)(4) AND 252(d)(3).

As noted above, wholesale rates for services offered for resale under § 251(c)(4) must be based on the retail price of the service, "excluding the portion thereof attributable to any marketing, billing, collection, and other costs that will be avoided by the local exchange carrier."[148] Avoided cost pricing maximizes economic efficiency by ensuring that the provider (incumbent LEC or reseller) that incurs the lowest cost for the provision of the "avoided" services (such as billing and end-user service) will in turn be able to charge its end-user customers the lower price. By the same token, efficiency will *not* be maximized if the LEC is required to exclude from the retail price costs that are not actually avoided by resale. Thus, § 251(d)(3) should not be interpreted to require the exclusion of costs that would not be avoided by resale, even if the costs in question are within one of the categories specifically mentioned in the section (marketing, billing, and collection).[149]

The amount of avoided may well vary from service to service and from carrier to carrier.[150] In this context, it would be unwise for the Commission to specify a single, universal avoided cost percentage or formula, or to impose in advance rigid rules governing what should

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[148] This section addresses paragraphs 178 to 188 of the NPRM.

[149] For example, the shift of units of service provided by a LEC from retail to wholesale channels would not necessarily reduce the LEC's retail advertising costs. Within broad ranges, a LEC may well spend as much to advertise to a smaller retail customer base as it would to advertise to a large base.

[150] This is not to say that each carrier should be required to set wholesale prices on a service-specific basis, since the data necessary to support such disaggregated pricing may not be readily available.

be highly fact-specific determinations. We believe that wholesale pricing of resold services should be left to the negotiation process and, where necessary, to State commission arbitration.

We consider in the following sections two important general issues relating to the determination of avoided cost: (a) variable v. fixed costs, and (b) the appropriate treatment of the cost onsets associated with resale.

A. Variable v. Fixed Costs

The historical costs of an incumbent LEC should have no relevance to the determination of its avoided cost, since by definition historical costs have already been incurred, and thus could not be affected by the shifting of supply from retail to resale channels. Only forward-looking economic costs can be considered as potentially avoidable.

Fixed costs, by definition, cannot be avoided as more output is supplied on a resale rather than a retail basis. Service-specific or shared fixed costs of the retail service — costs that could be avoided if the firm ceased production of retail service in its entirety — cannot be avoided because the altered sales relationship would not result in the cessation of any of the incumbent's services. Since only forward looking variable costs can be avoided, only those costs should be admitted to the "avoided cost" category for the purpose of calculating an efficient price for resold services.

Moreover, not all costs that are "variable" in some sense will necessarily be avoided through resale. Whether a cost will be avoided when a LEC provides a unit of service through a wholesale rather than a retail channel depends upon a careful analysis of the factors that cause the cost to be incurred. Costs that are fixed with respect to some output (*e.g.*, usage) might vary with another output (*e.g.*, the number of subscribers). The postage stamp on the monthly bill is an example of a cost that is fixed with respect to the volume of services supplied but that varies with the number of subscribers served — and thus would be avoided when a subscriber is served by a reseller.

B. Cost Onsets

As noted above, delivering services through wholesale (resale) channels rather than retail channels may enable a LEC to avoid some of the costs that it would otherwise incur. However, in general, a LEC will also need to incur a number of additional costs in order to serve the resale market. Some of these cost onsets are simply the costs of the investments that need be made in order to achieve cost avoidance. For example, one of the important reasons that a LEC can avoid costs by selling to resellers is that the LEC can receive orders from them through electronic interfaces rather than through individual, person-to-person contacts between end-user customers and sales representatives. However, in order to avoid those costs, the LEC would first need to invest in the establishment of the interfaces and related support systems. Other cost onsets are not directly related to cost avoidance, and simply represent the costs of serving resellers. The costs associated with reseller "liaison" personnel are an example of this category.

In either case, these cost onsets must be taken into account in the pricing of services offered for resale. (If they were not taken into account, economic inefficiencies would result, since one competitor — the LEC — would be bearing costs that are caused by the activity of another — the reseller.) These costs could either be taken into account by incorporating them into the basic wholesale pricing formula (i.e., by calculating the wholesale price as retail price less *net* avoided cost), or else by imposing them as separate rate elements to be paid by resellers.

C. Universal Service Funding

To the extent that LECs offer for resale services that qualify for universal service support, that support should be paid to the LEC and not the reseller. For example, if a LEC offers LifeLine service to a reseller at the normal retail LifeLine price, less a measure of avoided cost, then it is the LEC that would be bearing the burdens associated with the artificially low price of that service. Accordingly, it is the LEC that should be entitled to any funding made available pursuant to § 254 or parallel State funding provisions.

XI. RECIPROCAL COMPENSATION LEVELS FOR THE "TRANSPORT AND TERMINATION" OF CALLS MUST BE AGREED TO BY THE PARTIES AND MUST ENSURE RECOVERY OF THE RESPECTIVE CARRIER'S COSTS

Under Section 251(b)(5), the LECs have "a duty to establish reciprocal compensation arrangements for the transport and termination of telecommunications."[151] Under Section 252(d)(2) (which specifically refers to the § 251(b)(5) "reciprocity" duty), States are authorized to ensure that each interconnecting carrier recovers its costs in transporting and terminating traffic on its network facilities. In the NPRM, the Commission seeks comment on whether reciprocal compensation obligations apply to traffic exchanged between competing LECs, between independent telcos and LECs, and between LECs and CMRS providers; and on whether it is authorized to promulgate rules to guide the states in applying section 252(d)(2). In this regard, the Commission specifically inquires whether symmetrical compensation arrangements or Bill-and-Keep arrangements are appropriate under the Act. Finally, the

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[151] This section addresses paragraphs 226 to 244 of the NPRM.

Commission asks whether its adoption of "interim rules" for reciprocal compensation would be beneficial (NPRM ¶¶ 226-244).

NYNEX believes that Section 251 of the Act does not authorize the Commission to establish a mandatory regime here -- as elsewhere -- for compensation arrangements. Reciprocal compensation must be priced to ensure recovery of each carrier's "additional costs". Otherwise, it would be confiscatory. Reciprocal compensation does not require or even suggest that symmetrical compensation be utilized, although this may be a practical approach. Further, the Commission has no authority to mandate Bill-and-Keep arrangements. Such a compensation method can only be utilized if both parties to the interconnection agreement agree. Finally, interim rules will frustrate effective, mutual negotiations and should not be adopted.

A. Applicability

As discussed above, Section 251 is designed to impose obligations on LECs and incumbent LECs to advance competition within an exchange service area. Accordingly, the duty of reciprocal compensation applies to CMRS providers and LECs which provide competing service, but not to ICs or to service provided by independent telcos in adjacent exchange service areas.

The Commission asks whether "transport and termination" are separable in Sections 251(b)(5) and 252(d)(2), and can be priced differently, e.g., on a flat-rated basis (NPRM ¶ 231). Although these terms are inseparably used in the statute to describe a LEC-provided call terminating service;, the statute does not address appropriate rate structures, only rate levels.

Under the "pricing standards" applicable to "the transport and termination of traffic," the parties may reasonably determine that the rate structure may warrant some flat-rated elements, e.g., if the facility costs are largely non-traffic sensitive.[152] However, most importantly, the Commission may not lawfully direct such a structure since the rates are by statute to be set by the negotiated agreement of the parties subject to state approval and, if necessary, arbitration processes (Section 252).[153]

B. Rate Levels

The "pricing standards" of Section 252(d) are divided into three subsections. By its terms, only subsection (d)(2) is applicable to the LEC's obligation to enter into reciprocal compensation arrangements.[154] This subsection requires that each party recover the "additional costs" of transporting and terminating traffic on each other's network. The Commission expresses concern that the differences among the three statutory standards may cause confusion in the State review process or controversy among the parties as to their applicability (NPRM ¶ 232-234).

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152 Conversely, it has generally been thought that traffic-sensitive costs are most appropriately recovered in usage-based rates. Given the extent of such costs in switched "termination" services, it is expected that non-flat rated charges will generally be negotiated by the parties.

153 The LECs may also provide "interconnection" links under Section 251(c)(2) to join two networks. These will be subject to State approval (or arbitration) under the pricing standards of Section 252(d)(1). That is, the rate level shall be "based on cost . . . and [be] nondiscriminatory, and may include a reasonable profit."

154 Subsection (d)(1) requires that interconnection facilities and unbundled elements be priced at cost plus reasonable profit. Subsection (d)(3) requires that resale service be priced at the LEC's retail rate less avoided costs.

The Commission's concern is understandable but misplaced. As discussed above, the reciprocity obligation at issue only relates to the transport and termination of traffic, i.e., where another carrier purchases a service from the LEC to terminate a local exchange call to the LEC customer, or vice versa. Here, only Section 252(d)(2) applies.[155] That provision declares that "just and reasonable" terms and conditions for reciprocal compensation entail:

> "(i). . .the mutual and reciprocal recovery by each carrier of costs associated with the transport and termination in each carriers' network facilities of calls that originate on the network facilities of the other carrier; and
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> (ii) . . .such costs [are determined] on the basis of a reasonable approximation of the additional costs of terminating such calls."

The statute and legislative history do not further define the "additional cost" standard, except that in context the LECs are to fully recover their costs under Sections 251 and 252. Instead, the "defining" of this term will come from inter-carrier negotiations. Nor is it clear that it would be advantageous to establish a single methodology for States to use in reviewing such agreements, as contemplated by the Commission (NPRM ¶ 234). As noted above, rate variations between jurisdictions have historically been an accepted part of federal/state dual jurisdiction of transport and termination services under agreement. Indeed, there may be a reasonable basis for parties to embrace different cost methodologies in different areas, subject to the approval of the State regulatory authorities and review by an "appropriate federal district court" (Section 252(e)(6)). What is clear, however, is that the parties have the primary role in

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[155] Conversely, the statutory provisions governing interconnection and unbundled network elements involve a competing carrier's service to its own customers using LEC facilities.

defining these additional costs, a reasonable approach given that each is a *buyer and seller* of transport and termination services under their agreement.[156]

Next, the Commission indicates that the issue of statutory pricing standards raise particular questions about "rate symmetry" and "Bill-and-Keep" arrangements as possible forms of reciprocal payments. Rate symmetry as used by the Commission includes compensation arrangements for the transport and termination of traffic "in which the rate paid by an incumbent LEC to a competitor . . . is the same as the rate the incumbent LEC charges the competitor for the same service" (NPRM ¶ 235). As the Commission properly observes, identical payments are not required by the pricing standards of Section 252 (d)(2) which provides for each carrier's recovery of the costs of its own network facilities. This is unlikely to be the same amount for each carrier. However, while symmetry is not required by statute, it may result from the negotiation of the parties as a mutually adopted simplifying assumption. Thus, for example, the parties may decide that because LEC costs are better documented and mutually understood, these costs should serve as a "reasonable approximation" of both parties' "additional costs of terminating such calls" (Section 252 (d)(2)).

Similarly, the parties may agree upon an exchange of terminating traffic without payment to either carrier. These arrangements are referred to by the Commission as "Bill-and-

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[156] This point is given emphasis by the statutory admonition that Section 252(d)(2) "shall not be construed . . . to authorize the Commission or any State Commission to engage in any rate regulation proceeding to establish with particularity the additional costs of transporting and terminating calls...." (Section 252 (d)(2)(B)(ii)).

Keep" (NPRM ¶ 239). However, because "Bill-and-Keep" denies the LEC its statutory right to the recovery of its costs associated with transport and termination of traffic, such arrangements cannot be lawfully ordered by regulators absent the agreement of the parties. This is evidenced by the language in Section 252 (d)(2)(B)(ii) which allows parties to enter into reciprocal compensation arrangements that "waive" mutual recovery of costs (such as Bill-and-Keep arrangements).

Importantly, this language permits Bill-and-Keep arrangements (which would otherwise be unlawful under subsection Section 252 (d)(2)(A) as a denial of cost recovery) only where the parties "waive" their "mutual recovery" rights.[157] Much has been made in CC Docket No. 95-185 of the potential for "Bill-and-Keep" to be an equitable compensation arrangement under specific, limited circumstances: if costs are negligible; if they are equal for both carriers and traffic is balanced; or if they are unequal in precisely the converse proportion as traffic is imbalanced. In other circumstances, compelled "Bill-And-Keep" arrangements are confiscatory, serving to deny one entity its right to cost recovery. Without a showing here that these conditions prevail, "Bill-and-Keep" arrangements between LECs and others (like CMRS providers) must be left to the

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[157] Significantly, Black's Law Dictionary defines the term waiver as a "voluntary relinquishment of known rights" (4th Edition). A <u>compelled sacrifice</u> of these rights by regulatory action would obviously and unlawfully be the antithesis of such <u>voluntary relinquishments</u>. The provision is not included in the statute to enable State mandate (NPRM ¶ 243) but rather to explain that a voluntary agreement to exchange no payments may still meet the public interest standards of "mutual recovery" for reciprocal compensation.

agreement of the parties -- not to regulatory fiat -- as a matter of policy as well as a matter of law.[158]

C. Interim Rules

Finally, the Commission inquires whether it might be "desirable to establish an interim rule (such as Bill-and-Keep) to apply during ongoing negotiations or arbitrations (NPRM ¶ 244). Any such rule would gravely distort the negotiations process which is at the heart of Sections 251 and 252 since the entity favored by the "rule" would be disinclined to accept any lesser treatment, at least quickly and perhaps at all. Instead, Congress has provided for tight timetables to ensure that such agreements move rapidly along, as a far better approach.[159]

XII. THE ACT DOES NOT PRECLUDE DIFFERENTIAL TREATMENT AMONG CARRIERS

In the NPRM, the Commission tentatively concludes that the Act precludes differential treatment among carriers.[160] Under this conclusion, the Play or Pay regime adopted by the New York Public Service Commission ("NYPSC") would not be permitted.[161] The

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[158] The Commission recites arguments for and against "Bill-and-Keep" compensation arrangements (NPRM ¶¶ 241-242), but asks the parties not to reargue here their positions in CC Docket 95-185. However, inasmuch as the Commission indicates that it may incorporate arguments earlier made into this proceeding (NPRM ¶ 169), NYNEX specifically refers the Commission to its detailed showings that such arrangements are uneconomic (Affidavit of Dr. William Taylor) and beyond the power of the Commission to impose (Memorandum of Law), provided as attachments to NYNEX's Comments and Reply Comments, respectively, in that proceeding.

[159] See, e.g., Section 252 (e)(4) "Schedule For Decision."

[160] NPRM, ¶ 270.

[161] Play or Pay is discussed in ¶ 145 of the NPRM.

Commission also seeks comment on whether piece-parts of negotiated interconnection agreements or the entire agreement must be made available to carriers.

The 1996 Act, like the original Communications Act of 1934, permits reasonable differences in rates charged carriers under interconnection agreements so long as all similarly-situated carriers are treated alike. Play or Pay is thus consistent with the Act. It fosters non-discriminatory market-based competition and promotion of universal service, two of the goals of the Act.

A. "Play or Pay" Type Approaches Are Valid Under The Act

Some State commissions have established two-tier pricing structures for the termination of local calls exchanged by competing LECs. For example, the NYPSC requires LECs that are not "full-service, facilities-based" providers to pay standard carrier access rates to terminate local calls, while LECs that do provide a full range of services pay a lower rate based on the incremental cost of the call termination function.[162] Underlying the NYPSC orders establishing this rate structure are three principal policy judgments: (a) that consumers receive the greatest benefits in a market in which multiple facilities-based LECs offer a full range of services, rather than a market dominated by "niche providers" who simply cream skim by offering the most profitable services to the most profitable customers; (b) that a two-tier intercarrier compensation rate structure will encourage the development of such a market environment; and (c) that because full-service provision imposes burdens on "servers" that are not imposed on non-serving LECs, a two-tier intercarrier rate structure levels the competitive

[162] The "full service" providers who pay the lower termination rate under the NYPSC's pricing construct are sometimes referred to as "players" or "servers".

playing field. In short, companies operating as "servers" would pay lower interconnection rates in recognition of the additional burdens associated with being a server, and in order to incent firms to be servers rather than non-servers.

As explained below, such policies and the rate structures that support them are fully consistent with the Act.

1. New York's "Play or Pay" Rulings

In a June 1994 order (the "ACC Order"),[163] the NYPSC considered a tariff filing under which a CLEC, ACC Syracuse Telecom Corp., proposed to offer local dial tone service to business customers but to postpone its planned offering of local dialtone service to residence customers (including an offering of LifeLine service). Although allowing the postponement, the Commission noted that "*concerns about competitive equity* are raised by ACC's proposal to initially target only profitable business customers because New York Telephone Company will continue to bear all universal service obligations associated with the provision of residence and LifeLine service."[164] "To accommodate this situation," the NYPSC Staff recommended and ACC agreed to an arrangement under which the call termination rates paid by ACC would equal NYT's switched carrier access charges, together with certain additional rate elements, while NYT would pay lower, less contributory rates.

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[163] Case 93-C-0905, *Original Tariff Filing of ACC Syracuse Telecom Corp. to Provide and Resell All Forms of Switched and Non-Switched Telephone Service On An Intercity and Intracity Basis in New York State*, June 15 memorandum from the Communications Division to the Commission (approved as recommended and so ordered by the Commission effective June 29, 1994).

[164] ACC Order at 3 (emphasis supplied); see also id. at 13.